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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 246

FREDERICK S. DEITRICK, Receiver of the Boston-Continental National Bank, *Petitioner*,

v.

THOMAS E. GREANEY, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

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v.

THOMAS E. GREANEY, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, Frederick S. Deitrick, receiver of the Boston-Continental National Bank by appointment of the Comptroller of the Currency, prays that a writ of certiorari issue to review the final decree of the United States Circuit Court of Appeals for the First Circuit rendered in the above case on March 25, 1939.

Opinions Below.

The opinion of the District Court of the United States for the District of Massachusetts appears on pages 13 to 17 of the record and is reported in 23 F. Supp. 758. The opinion of the Circuit Court of Appeals modifying the original decree of the District Court appears on pages 77 to 90 of the record and is reported in 103 F. (2d) 83.

Jurisdiction.

Jurisdiction is conferred upon this Court to review this cause by writ of certiorari by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (U. S. C. title 28, sec. 347).

The decree of the Circuit Court of Appeals for the First Circuit sought to be reviewed was entered on March 25, 1939 (R. 90-91). A petition was filed with the Honorable Felix Frankfurter, Associate Justice of the Supreme Court of the United States, for an extension of time within which to file petition for writ of certiorari in this case. Under date of June 2, 1939, an order was entered by Mr. Justice Frankfurter granting an extension of 35 days from June 25, 1939, within which to file a petition.

Question Presented.

Whether the receiver of an insolvent national bank may enforce a promissory note given to the bank by a director thereof for the purpose of concealing from the national bank examiners an illegal acquisition by the bank of shares of its own stock, where such note was given with a secret oral understanding that it was not to be enforced by the bank.

Summary Statement of Matters Involved.

In April, 1930, Boston National Bank purchased 190 shares of its own stock, in violation of the National Bank Act (sec. 5201 of Rev. Stat. of 1873 (U. S. C. title 12, sec. 83)) (R. 13). In order to conceal this illegal acquisition and owner-

ship from the national bank examiner (R. 30), and avoid the consequences thereof, a scheme was devised whereby the stock would be removed from the assets of the bank and replaced by a note of some person (R. 13).

Defendant Greaney was a shareholder of Boston National Bank (R. 56) and a director thereof from 1923 until the day it closed (R. 30). After conferring with Ulin, the president of the bank, Greaney was conversant with the plan for the disposition of the 190 shares. He thereupon prevailed upon one Karnow to execute a note in the amount of $23,500, payable to the bank. Karnow's note was discounted by the bank and he was given a check drawn on the bank in the amount of $23,203.14. In accordance with the agreement between the parties, Karnow deposited this check in another bank to the credit of Director Greaney. Greaney then issued his own check drawn against the deposit in the other bank payable to Boston National Bank for the full amount of the deposit. This check was delivered to Boston National Bank as the purchase price of said stock and the shares of stock were then transferred on the books of the bank to Greaney (R. 13-14). When Karnow's note became due he was persuaded to renew it and shortly thereafter he caused the stock to be transferred on the bank's records to his own name and he took actual possession of the new certificates (R. 14).

In the fall of 1930, a consolidation of Boston National Bank and Continental National Bank was effected, and the 190 shares of Boston National Bank stock were converted into 684 shares of stock of the consolidated bank. In connection with this consolidation, Ragan (who became president of the consolidated bank), together with one Balter, agreed to purchase these shares, and they gave the bank their three notes aggregating $24,000 in payment therefor, the stock to be delivered as the notes were paid. One of these (for $9,500) was paid; this amount was credited to Karnow's note; and a proportionate number of the shares were transferred from Karnow's name to the purchasers (R. 14-15).

Because of Karnow's insistence that he be relieved from liability, Greaney gave the consolidated bank his own note for $14,553.66, and this note was discounted by the bank and its check used to discharge the Karnow note (R. 15). At Greaney's request the shares were transferred into the name of one Mahoney, who had no knowledge of the transaction at any time prior to the commencement of this suit (R. 15.) The certificates in Mahoney's name were delivered to Greaney (R. 21).

In December, 1931, Boston-Continental National Bank closed its doors, and a receiver was appointed by the Comptroller of the Currency to administer its affairs (R. 14). At that time, as theretofore, Greaney's note was held by the bank among its regular assets, and was wholly unpaid (R. 26). On July 11, 1932, the Comptroller of the Currency levied a 100 per cent assessment upon all owners of stock of the bank. The assessment on the shares here involved has not been paid (R. 21-22).

In 1935, the petitioner sued Greaney, Karnow and Mahoney for the amount of the unpaid assessment, with interest, and sued Greaney and Karnow for the amount of the unpaid note, with interest (R. 4). The decree of the District Court held Greaney liable for the amount of the note and the amount of the assessment, both with interest, and dismissed the bill of complaint with respect to Karnow and Mahoney (R. 12). Greaney appealed, and the Circuit Court of Appeals affirmed the decree of the District Court with respect to Greaney's liability for the stock assessment, but reversed the decree as to liability on the note (R. 90).

Specification of Errors to be Urged.

The Circuit Court of Appeals erred:

1. In failing to apply the law of Massachusetts to the question of Greaney's liability on his note.

2. In holding that where a note is given to a national bank by a director thereof in order to conceal from the national

bank examiners and the Comptroller of the Currency its true condition and its commission of illegal acts, the maker of such note may set up as a defense that the note was given for the accommodation of the bank and lacked consideration.

3. In holding that the receiver of an insolvent national bank is barred from enforcing a note because of the bank's participation in an unlawful act connected with the giving of the note.

4. In holding that the receiver of an insolvent national bank, who represents primarily the depositors and other creditors of the bank, is in no better position, with respect to recovery on such a note, than the bank itself would have been, suing as a solvent institution.

5. In failing to hold that the receiver of an insolvent national bank may enforce a note given to the bank by a director thereof in order to conceal from the national bank examiners an illegal acquisition by the bank of shares of its own stock.

6. In failing to affirm the decree of the District Court holding Greaney liable on his note.

Reasons for Granting the Writ.

1. The Circuit Court of Appeals has decided an important question of Massachusetts law in a way in conflict with the applicable decisions of the Supreme Judicial Court of Massachusetts. The question here presented is simply whether the receiver of a bank, as the representative of its depositors and other creditors, is entitled to enforce a promissory note knowingly given to the bank by one of its directors for the specific purpose of deceiving the public examining authorities with respect to the condition of the bank, and to conceal the fact that the bank, its directors, and its officers had violated the statute forbidding it to purchase shares of its own stock. Since the transactions in

question took place in Massachusetts, the interpretation, validity, and enforceability of the note are governed by the law of that State. *Erie R. Co.* v. *Tompkins*, (1938) 304 U. S. 64; *Gaston, Williams & Wigmore* v. *Warner*, (1922) 260 U. S. 201; *Marine Nat. Exch. Bk.* v. *Kalt-Zimmers Mfg. Co.*, (1934) 293 U. S. 357; *Reconstruction Finance Corporation* v. *O'Keefe*, (C. C. A. 3d, 1938) 98 F. (2d) 820; *Reno Nat. Bank of Reno, Nev.* v. *Seaborn*, (C. C. A. 9th, 1938) 99 F. (2d) 482; *Cherry* v. *Sprague*, (1904) 187 Mass. 113, 72 N. E. 456; *Walling* v. *Cushman*, (1921) 238 Mass. 62, 130 N. E. 175; *Sterrett* v. *Stoddard Lumber Co.*, (1935) 150 Ore. 491, 46 P. (2d) 1023; *Jefferis* v. *Kanawha Fuel Co.*, (1923) 182 Wis. 203, 196 N. W. 238. See *Conflict of Laws Restatement, secs.* 332, 336, 347, 358.

The controlling decision in Massachusetts is *Prudential Trust Co.* v. *Moore*, (1923) 245 Mass. 311, 139 N. E. 645. In that case directors of the bank executed and delivered promissory notes to it in order to replace certain excessive loans on the books of the bank and thereby "to prevent the closing of the bank", the makers having been assured by the president of the bank "that they were really assuming no liability at all". Thereafter, the bank was closed, insolvent, with these notes ostensibly among its assets. The Supreme Judicial Court of Massachusetts held the directors "estopped from denying the legal validity of these notes which the bank commissioner is now attempting to collect for the benefit of creditors of the bank". The opinion stated that it would be unjust and fraudulent to permit these directors "to now plead the invalidity of the very securities by which they induced others to make and leave deposits with the bank". Accordingly, the court held that the public officials representing the bank's depositors and other creditors were entitled to enforce the notes. Accord: *International Trust Co.* v. *Wattendorf*, (1926) 256 Mass. 323, 152 N. E. 306.

The pertinent facts of this case are almost identical with those of *Prudential Trust Co.* v. *Moore* and *International*

Trust Co. v. *Wattendorf*, both *supra*, even to the extent that Greaney, the maker of the note, was a director of the insolvent bank, as were the defendants in those cases. In fact, the circumstances of the present case even more strongly call for imposing liability on the maker of the note: In the *Prudential Trust Co.* case the directors were told by the bank president that "the situation involved simply a technical question" and could be cleared up in a few days, whereas in this case Greaney, the director, was entirely aware that the bank had acquired its own stock in violation of law and desired to conceal this fact from the bank examiners, the Comptroller of the Curreney, and through them the depositors and other creditors of the bank.

Whether negotiable instruments given to a banking institution in the circumstances of this and similar cases, which are valid on their face and have been included among the purported assets of the bank in reliance upon which deposits have been made and continued by innocent members of the public, shall be enforceable, upon the bank's insolvency, for the benefit of such depositors, is a question of great importance with respect to the safety and proper management of the banking facilities of any community.

That this question is a matter of unusual public concern has been recognized increasingly in recent years, as indicated by the tendency of courts to rely less upon the technical doctrine of estoppel, but rather to base the imposition of liability in these cases upon the broad principle of public policy that the stability of banks and popular confidence in our banking structure must not be jeopardized by spurious transactions of this character. This change in emphasis is clearly reflected in two important opinions handed down during the current year. In *O'Keefe* v. *Equitable Trust Co.*, (C. C. A. 3d, 1939) 103 F. (2d) 904, 908, the court said:

> "And again, a fortiori, will the policy apply to banks, institutions whose raison d'etre should guarantee the identity of reality and appearance. As a distin-

guished court and a learned professor of law put it: 'The state cannot sanction any device intended to give a false appearance to a transaction or increase the apparent stability of a bank. * * * Public policy requires that a person who, for the accommodation of the bank executes an instrument which is in form a binding obligation, should be estopped from thereafter asserting that simultaneously the parties agreed that the instrument should not be enforced.' Mount Vernon Trust Co. v. Bergoff, 272 N. Y. 192, 197, 5 N. E. (2d) 196, 197.

"* * * It is interesting to observe that the later cases place their decisions squarely on the ground of public policy and do not strain at an enlarged concept of consideration or an hypothetical estoppel."

And in *Rothschild v. Manufacturers Trust Co.*, (1939) 279 N. Y. 355, 18 N. E. (2d) 527, 529, the Court of Appeals of New York forcibly enunciated the same principle:

"An agreement, valid and enforcible if made by an ordinary corporation or business, may, by reason of public policy, be void and unenforcible against a banking institution. Thus, where a bank brings suit on a promissory note, the defendant may not plead lack of consideration and an agreement not to enforce the instrument, since the defendant knows or was chargeable with knowledge that the note might be used to conceal the actual transaction. * * * The public policy behind these rulings is that the stability of banks is a matter of such public concern that the State should not sanction any device intended to give a false appearance to a transaction or increase the apparent stability as contrasted with the true condition of a bank. It may be noted here that this rule of public policy in no wise depends upon the solvency or insolvency of the bank. * * *"

Accordingly, the action of the Circuit Court of Appeals for the First Circuit in failing to follow the controlling decisions of Massachusetts and to affirm the decree of the District Court holding Greaney liable on his note should be reviewed by this Court.

2. In addition to the conflict between the decision below and the decisions of the Supreme Judicial Court of Massachusetts, the decision below is in conflict with the principle applied by this Court in *Texas & Pacific Ry.* v. *Pottorff*, (1934) 291 U. S. 245, and with the decisions of the Circuit Courts of Appeals for the Fourth and Fifth Circuits in *Federal Reserve Bank* v. *Crothers*, (1923) 289 Fed. 777, and *Bohning* v. *Caldwell*, (1925) 10 F. (2d) 298 (cert. den. (1926) 271 U. S. 663), respectively. Accord: *Pauly* v. *O'Brien*, (C. C. Calif., 1895) 69 Fed. 460; *Utley* v. *Clarke*, (N. D. N. Y., 1936) 16 F. Supp. 435. See *McCandless, Receiver* v. *Furland*, (1935) 296 U. S. 140, 159, 160; *O'Keefe* v. *Equitable Trust Co., supra.*

The decision in the *Pottorff* case, *supra*, upheld the right of a receiver of an insolvent national bank to recover securities which the bank had pledged to secure deposits by the defendant railroad. This Court rejected the argument that the receiver was solely the representative of the bank and as such could "have no greater right" than the bank. The Court recognized that the receiver of an insolvent national bank may in some circumstances be entitled to enforce rights which the bank as a solvent institution could not have enforced, stating that "even if the bank would have been estopped from asserting lack of power, its receiver would be free to challenge the validity of the pledge".[1] (291 U. S. at 260.)

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[1] It should be mentioned that some of the leading decisions on this question by the highest courts of the several states reflect the tendency to hold such a note as that involved in this case enforceable not only by the receiver, but by the bank itself. *Rogers* v. *First State Bank*, (1926) 79 Colo. 84, 243 Pac. 637; *Cedar State Bank* v. *Olson*, (1924) 116 Kan. 320, 226 Pac. 995; *State Bank of Moore* v. *Forsyth*, (1910) 41 Mont. 249, 108 Pac. 914; *Bay Parkway Nat. Bank* v. *Shalom*, (1936) 270 N. Y. 172, 200 N. E. 685; *First National Bank* v. *Boxley*, (1927) 129 Okla. 159, 264 Pac. 184; *Bangor Trust Co.* v. *Christine*, (1929) 297 Pa. 64, 146 Atl. 545; *Farmers & Merchants' State Bank* v. *Perry*, (1925) 186 Wis. 93, 202 N. W. 179; see *Brannan, Negotiable Instruments Law* (6th ed. 1938) 454-457. However, that somewhat more difficult question does not arise in this case.

McCandless, Receiver v. *Furland, supra*, raised the question of the right of the receiver of an insolvent corporation to recover from its promoters unconscionable profits obtained by selling it land and marketing its securities. This Court held that the rights of creditors rose superior to a fraudulent attempt by the corporation and its insiders to impair its assets. "If the shareholders and the directors had combined with the promoters to despoil the corporation and defeat the remedies of creditors by a gift of half the assets, the gift could have been annulled either by the creditors directly or in their behalf by a receiver" (296 U. S. at 159). Again it was recognized that the creditors of a corporation, represented by its receiver, can assert rights which might not be enforceable by the corporation as a going concern:

> "There is no occasion to consider whether the corporation itself at the instance of new shareholders would be permitted to disaffirm the fraud and maintain a suit in equity for appropriate relief. We put that question by. *Enough that the receiver has the requisite capacity.*" (296 U. S. at 160. Italics ours)

In *Bohning* v. *Caldwell, supra*, the receiver of an insolvent national bank sued several of its directors on a note made by them and given to the bank to take the place of certain doubtful or worthless assets; "none of the makers of the note considered they would ever be called upon to pay it". The court held the note to be enforceable on the ground that since the makers of the note were *directors and stockholders* of the bank, there was sufficient consideration for the note, and also that the directors were estopped to deny consideration.

Federal Reserve Bank v. *Crothers, supra*, is particularly significant. The president of a national bank had persuaded Crothers to give the bank his note for $6,000 "to take the place of an equivalent of electric light plant bonds [constituting an excessive investment] for the satisfaction of

the bank examiner". The bank failed, and the court held its receiver entitled to enforce the note. Counsel for the defendant relied upon *Rankin* v. *City Nat. Bank*, (1908) 208 U. S. 541. Although the court (Taft, Circuit Justice, Woods, Circuit Judge, and Groner, District Judge) distinguished the *Rankin* case, their decision indicates a disposition to confine the holding in that case to the particular facts there presented.

The *Rankin* case, *supra*, which concerned a legal transaction between two banks, is not controlling in this case, where the defendant was a **director** of the insolvent bank, **fully acquainted with its affairs and the illegal transaction which he was assisting to conceal, despite the fiduciary duty which he owed to its depositors.** It is to be noted that the *Rankin* case has not been cited by this Court in over thirty years, except in *Deitrick* v. *Standard Surety Co.*, (1938) 303 U. S. 471, where the decision was based primarily on the condition of the pleadings.

The overwhelming weight of authority of the state courts concurs in holding that negotiable instruments given to banks in the circumstances here presented are enforceable by the receivers thereof.[2]

Murphy, Receiver v. *Gumaer*, (1902) 18 Colo. App. 183, 70 Pac. 800.
Ashley v. *Rowe*, (1931) 101 Fla. 110, 133 So. 551.
Niblack v. *Farley*, (1919) 286 Ill. 536, 122 N. E. 160.
Iglehart v. *Todd*, (1931) 203 Ind. 427, 178 N. E. 685.
Hayes v. *Addy*, (1934) 139 Kan. 481, 32 P. (2d) 243.
Denny v. *Fishter*, (1931) 238 Ky. 127, 36 S. W. (2d) 864.
New v. *Page*, (1924) 144 Md. 606, 125 Atl. 403.
Prudential Trust Co. v. *Moore*, (1923) 245 Mass. 311, 139 N. E. 645.

[2]Although only one case is cited from each state the highest court of which has passed on this question, it should be noted that in a number of jurisdictions the principle has been reiterated and applied by the highest and intermediate appellate courts in a number of other cases.

Parker v. *Parker*, (1938) 287 Mich. 49, 282 N. W. 897.
German-American Finance Corp. v. *Merchants & Mfrs. Bank*, (1929) 177 Minn. 529, 225 N. W. 891.
Bank of Slater v. *Union Station Bank*, (1920) 283 Mo. 308, 222 S. W. 993.
State Bank of Moore v. *Forsyth*, (1910) 41 Mont. 249, 108 Pac. 914.
Harrington v. *Connor*, (1912) 51 Neb. 214, 70 N. W. 911.
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Bay Parkway Nat. Bank v. *Shalom*, (1936) 270 N. Y. 172, 200 N. E. 685.
Vallely v. *Devaney*, (1923) 49 N. D. 1107, 194 N. W. 903.
State, ex rel. Lattanner v. *Hills*, (1916) 94 Ohio St. 171, 113 N. E. 1045.
First National Bank v. *Boxley*, (1927) 129 Okla. 159, 264 Pac. 184.
Putnam v. *Chase*, (1923) 106 Ore. 440, 212 Pac. 365.
Lyons v. *Benney*, (1911) 230 Pa. 117, 79 Atl. 250.
Arthur v. *Brown*, (1912) 91 S. C. 316, 74 S. E. 652.
Shaw v. *Borchers*, (Texas, 1930) 46 S. W. (2d) 967.
West Rutland Tr. Co. v. *Houston*, (1932) 104 Vt. 204, 158 Atl. 69.
Moore v. *Kildall*, (1920) 111 Wash. 504, 191 Pac. 394.
Schwenker v. *Teasdale*, (1931) 206 Wis. 275, 239 N. W. 434.

See also:

Day v. *Farmers' & Merchants' Bank*, (1934) 229 Ala. 372, 376, 377, 157 So. 439, 443, 444.
Riches v. *Hadlock*, (1932) 80 Utah 265, 288, 15 P. (2d) 283, 292.
Webb v. *Pleasants*, (1926) 144 Va. 516, 519, 132 S. E. 175, 176.
Brannan, Negotiable Instruments Law (6th ed. 1938) 458-460.

As indicated hereinabove, the question presented by this case is one of great importance with respect to the stability and proper management of the institutions which make up

our public banking system. In order to protect the public from a practice which, if permitted, would dangerously impair the capital of national banks, the National Bank Act prohibits national banks from purchasing shares of their own capital stock, as was done in this case. In fact, the danger is considered so great that Congress has specifically authorized the Comptroller of the Currency to appoint a receiver to close up the business of any bank which holds shares of its stock in violation of this section of the law. Section 5201 of Rev. Stat. of 1873 (U. S. C. title 12, sec. 83).

Without doubt, the most effective method employed by the Government to protect the public against just such hazardous departures from safe and sound banking practice is the conduct of thorough periodic examinations of national banks by bank examiners appointed by the Comptroller. Section 5240 of Rev. Stat. of 1873, as amended (U. S. C. title 12, sec. 481). A rule of law permitting a **director** of a national bank to escape liability to the depositors and creditors of such bank (or a receiver acting for their benefit), where such director has conspired with other bank officials to deceive the Comptroller and his examiners, and through them the public, as to the true condition of the bank, and to conceal from them the commission of a highly dangerous violation of the banking laws, by placing among the assets of the bank an obligation *prima facie* valid and enforceable but subject to a secret agreement that it was not to be enforced, would defeat the entire purpose of the regulatory statutes and would be in conflict with sound public policy.

Accordingly, the action of the Circuit Court of Appeals for the First Circuit in departing from the controlling principles recognized in the decisions of this Court, in other Circuit Courts of Appeals, and in the overwhelming majority of the state courts which have passed upon this question, should be reviewed by this Court.

Conclusion.

For the reasons stated, it is respectfully submited that this application for a writ of certiorari should be granted.

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